in the claims process, as there is no downside to filing a claim and many investors have received full compensation for their losses through this process.

**DOC Enforcement Activity.** On November 14, DOC announced its intent to fine TakeCare Health Plan $500,000 for multiple violations of the Knox-Keene Health Care Service Plan Act of 1975, including failure to provide appropriate access to quality medical care which jeopardized the life of a young patient. In its accusation and petition, the Department alleged, among other things, that TakeCare failed to provide Carley Christie, a young girl diagnosed with a rare and life-threatening childhood cancer called Wilms' tumor, with appropriate access to a qualified pediatric surgeon to remove her malignant tumor, in accordance with professionally recognized standards of practice; retaliated against Carley's parents for independently seeking to obtain the services of a qualified pediatric surgeon to treat their daughter; and failed to demonstrate that its refusal to provide these medical services was unhindered by fiscal considerations. The Department also alleged that, in addition to assessing the $500,000 fine, it also directed TakeCare to take a number of steps to assure that the problems identified in the Christie case are not repeated. TakeCare intends to appeal the fine by requesting an administrative hearing.

On December 6, the Commissioner announced a major enforcement action against high-tech scams targeting Individual Retirement Accounts (IRAs). After a year-long, multi-state investigation, DOC filed ten civil actions, issued fifty desist and refrain orders, issued 41 subpoenas, and referred seven cases for criminal prosecution. According to DOC, this is by far the largest enforcement DOC has ever undertaken, including 426 target entities and individuals and involving offerings amounting to over $850 million.

The Commissioner warned investors to be wary of investment offerings claiming huge returns and little risk. In many instances, investors were falsely told that they were investing in "IRA-approved" offerings endorsed by the Internal Revenue Service (IRS) when, in fact, the IRS does not "qualify," "review," or "approve" individual investments. These offerings were targeted through television commercials and written sales materials. According to the civil complaints, the illicit offerings were promoted as high-tech communications services, and other high-tech communications services. The Department worked with the National White Collar Crime Center (NWCCC) in Richmond, Virginia, a federally-funded law enforcement project, to create a database of investigative and enforcement information on the scams, and sent questionnaires to 7,000 investors in 141 high-tech offerings nationwide. The research showed that these high-risk investments were directed at a group deemed least suitable for such, as these investors were looking for safe investments to provide income in their retirement years. Instead, company officials paid themselves huge fees, leaving little for project development and investors with little if any chance to earn a return on their investment. Commissioner Mendoza warned that high-tech deals can be inherently risky because of the rapid changes in technology and that promises of high returns with little risk should be looked upon with great skepticism.

**LEGISLATION**

**AB 46 (Hauser),** as introduced December 12, would reorganize and expand the scope of the law relating to homeowners' association board of directors' meetings by creating the "Common Interest Development Open Meeting Act." This bill would set forth the rights and responsibilities of board members and association members with respect to meetings; the bill would also designate certain activities in which a board may engage that do not fall within the definition of a meeting. [A. & CD]

**AB 73 (Friedman),** as introduced December 21, would prohibit health care service plans and disability insurers from awarding bonus compensation to any employee on the basis of that employee's performance in denying authorization or payment for costly services. This bill would require the Commissioner of Corporations to establish and maintain a toll-free telephone number for the purpose of receiving complaints and inquiries regarding health care service plans. [A. Health]

**LITIGATION**

In Murray, et al. v. Belka, et al., No. 740706 (Orange County Superior Court), filed on December 30, a group of investors in failed First Pension Corporation alleges that, as a lawyer in the mid-1980s, DOC Commissioner Gary Mendoza misled the public. The complaint alleges that while he was a lawyer at Latham & Watkins in Newport Beach, Mendoza prepared securities offerings for a First Pension entity in flagrant violation of state securities laws and to have committed breaches of fiduciary duty and fraud. Specifically, the suit alleges that Mendoza provided legal services to the operators of First Pension from 1992 until shortly before his appointment as DOC Commissioner in July 1993. The suit claims that Mendoza and the other defendants failed to disclose facts concerning the true nature of the limited partnership units sold by the defendants in documents provided to investors on a limited partnership offering sold in the mid-1980s. Commissioner Mendoza called the lawsuit "absurd and contemptible."

At this writing, the California Supreme Court has not yet scheduled oral argument in its review of the Second District Court of Appeal's decision in People v. Charles Keating. 16 Cal. App. 4th 280 (1993). In its ruling, the Second District affirmed a jury verdict in which the former savings and loan boss was found guilty of defrauding 25,000 investors out of $268 million by persuading them to buy worthless junk bonds instead of government-insured certificates. [12:4 CRLR 120-21; 12:2 & 3 CRLR 169] In his appeal (No. S033855), Keating primarily challenges the trial court's jury instructions stating that he could be convicted under theories that he was either the direct seller of false securities in violation of Corporations Code sections 25401 and 25540, or a principal who aided and abetted the violations. The issue is whether aiding and abetting of a section 25401 crime statutorily exists; Keating claims that criminal liability is restricted to direct offerors and sellers, and that the evidence failed to prove he personally interacted with any of the investors.

**DEPARTMENT OF INSURANCE**

Commissioner: Charles Quackenbush
(415) 904-5410
Toll-Free Complaint Number: 1-800-927-4357

Insurance is the only interstate business wholly regulated by the several states, rather than by the federal government. In
California, this responsibility rests with the Department of Insurance (DOI), organized in 1868 and headed by the Insurance Commissioner. Insurance Code sections 12919 through 12931 set forth the Commissioner’s powers and duties. Authorization for DOI is found in section 12906 of the 800-page Insurance Code; the Department’s regulations are codified in Chapter 5, Title 10 of the California Code of Regulations (CCR).

The Department’s designated purpose is to regulate the insurance industry in order to protect policyholders. Such regulation includes the licensing of agents and brokers, and the admission of insurers to sell in the state.

In California, the Insurance Commissioner licenses approximately 1,300 insurance companies which carry premiums of approximately $63 billion annually. Of these, 600 specialize in writing life and/or accident and health policies.

In addition to its licensing function, DOI is the principal agency involved in the collection of annual taxes paid by the insurance industry. The Department also collects more than 170 different fees levied against insurance producers and companies.

The Department also performs the following functions:

1. regulates insurance companies for solvency by tri-annually auditing all domestic insurance companies and by selectively participating in the auditing of other companies licensed in California but organized in another state or foreign country;
2. grants or denies security permits and other types of formal authorizations to applying insurance and title companies;
3. reviews formally and approves or disapproves tens of thousands of insurance policies and related forms annually as required by statute, principally related to accident and health, workers’ compensation, and group life insurance;
4. establishes rates and rules for workers’ compensation insurance;
5. preapproves rates in certain lines of insurance under Proposition 103, and regulates compliance with the general rating law in others; and
6. becomes the receiver of an insurance company in financial or other significant difficulties.

The Insurance Code empowers the Commissioner to hold hearings to determine whether brokers or carriers are complying with state law, and to order an insurer to stop doing business within the state. However, the Commissioner may not force an insurer to pay a claim—that power is reserved to the courts.

DOI has over 800 employees and is headquartered in San Francisco. Branch offices are located in San Diego, Sacramento, and Los Angeles. The Commissioner directs 21 functional divisions and bureaus.

The Underwriting Services Bureau (USB) is part of the Consumer Services Division, and handles daily consumer inquiries through the Department’s toll-free complaint number. It receives more than 2,000 telephone calls each day. Almost 50% of the calls result in the mailing of a complaint form to the consumer. Depending on the nature of the returned complaint, it is then referred to Claims Services, Rating Services, Investigations, or other sections of the Division.

Since 1979, the Department has maintained the Bureau of Fraudulent Claims, charged with investigation of suspected fraud by claimants. The California insurance industry asserts that it loses more than $100 million annually to such claims. Licensees currently pay an annual assessment of $1,000 to fund the Bureau’s activities.

**MAJOR PROJECTS**

**Quackenbush Elected Commissioner.** On November 8, California voters elected Republican Assemblymember Charles Quackenbush as the new Insurance Commissioner. Quackenbush, whose campaign was heavily financed by the insurance industry, rode the so-called “Republican wave” into office by defeating Democrat Art Torres, chair of the Senate Insurance Committee. In his inauguration speech on January 4, Quackenbush promised to seek repeal of Insurance Code section 10081, which requires all insurers who sell homeowners insurance in California to offer earthquake insurance—a move the insurance industry has been seeking since the January 1994 Northridge earthquake. [14/4 CRLR 122–23] Quackenbush’s next action was to withdraw all regulations which had been adopted by his predecessor, Democrat John Garamendi, and were pending review and approval at the Office of Administrative Law (see below).

**Garamendi Ends Term by Issuing Proposition 103 Rollback Orders.** On November 22, then-Commissioner John Garamendi ordered 28 insurers to fulfill their “rollback” obligations under Proposition 103, which was enacted by the electorate in November 1988. With interest, the ordered rebates total $1.25 billion. In August 1994, following interminable legal challenges by the insurance industry, the California Supreme Court unanimously affirmed the constitutionality of Garamendi’s regulations which implement the initiative’s rollback provision and set forth the formula under which they should be calculated (see LITIGATION).[14/4 CRLR 129–131]

However, the rollback orders simply trigger the insurers’ rights to challenge Garamendi’s calculations or otherwise seek relief through a hearing before a DOI administrative law judge or the courts. More significantly, most of the insurers subject to the November 22 orders simply failed to comply with them prior to Garamendi’s departure from office, and are now free to negotiate a settlement of their rollback obligation with new Commissioner Quackenbush, whose campaign they financed. In his January 4 inauguration speech, Quackenbush promised that all remaining Proposition 103 rollback checks would be in the mail within six months.

**DOI Releases Analysis of Weighting Proposition 103 Auto Rating Factors.** On December 27, the Department’s Office of Policy Research released a report entitled Impact Analysis of Weighting Auto Rating Factors to Comply with Proposition 103, which is the culmination of eighteen months of research, study, and analysis of public hearings held by DOI.

One of the primary goals of Proposition 103 was elimination of so-called “territorial rating,” whereby insurers base auto rates on the policyholder’s residential ZIP code instead of his/her driving record. Proposition 103 requires auto rates to be based primarily on three “mandatory” factors (the insured’s driving safety record, the number of miles driven annually, and the number of years of experience the driver has been licensed to drive in any jurisdiction) and any “optional” factors which the Commissioner adopts by regulation. To preclude insurers from “weighting” particular factors (such as geographic residence) so heavily that they would outweigh the mandatory factors, Proposition 103 requires insurers to apply the factors in “decreasing order of importance” and requires the Insurance Commissioner to adopt regulations which “set forth the respective weight to be given each factor in determining automobile insurance rates and premiums.” Insurance Code section 1861.02(a).

During the years after its enactment, two Insurance Commissioners (Gillespie and Garamendi—see below) adopted their own sets of regulations defining the mandatory factors and identifying 10–20 optional factors which insurers may use as the basis for calculating auto premium rates; Commissioner Gillespie additionally adopted a “tempered” weighting methodology which was subsequently...
challenged by the insurance industry and invalidated by then-Los Angeles County Superior Court Judge Miriam Vogel in March 1990. [10:2 & 3 CRLR 140] Gillespie subsequently adopted an "interim" emergency weighting methodology regulation in August 1990 [10:4 CRLR 123], but that regulation merely required insurers to use a "sequential analysis" without defining that term or specifying how the rating factors were to be weighted; as such, they do not comply with Proposition 103's directive. That "interim" emergency regulation—which was only supposed to remain in effect for 120 days—has been readopted as such on at least fifteen occasions and is still in effect at this writing. Section 2632.7, Title 10 of the CCR.

In July 1993, Commissioner Garamendi commenced a comprehensive rulemaking proceeding to adopt his own definitions of the mandatory and optional auto rating factors; within the rulemaking were four optional weighting methodologies upon which the Commissioner sought public comment. [13:4 CRLR 111–12] Following a symposium at which expert actuarial testimony was presented on the weighting alternatives, Garamendi concluded that extensive research was necessary before promulgating a regulation. Thus, in August 1993, he separated out section 2632.7 from the rest of the auto rating factors rulemaking package (see below) and directed DOI's Office of Policy Research to launch a long-term actuarial study to determine the most appropriate weighting methodology.

The purpose of DOI's study was to analyze the impact of the application of various weighting methodologies to determine "premium variation," or the increase/decrease in current premium amount depending on how the weight of a rating factor is measured. For example, the mileage rating factor could be divided into five categories (very low, low, average, high, and very high annual mileage). Properly weighted, policyholders falling into the low and very low mileage categories would receive discounts, those in the high and very high categories would be surcharged, and those in the average category would see no change in their current premium based upon that factor. The amount of discounts and surcharges associated with a rating factor affect its ability to influence the final premium paid by consumers. The weight of a rating factor is the measurement of its influence on premium.

DOI's study focused on two weighting approaches: the "Single Omit" method and the "Average Class" method. The Single Omit method calculates the weight of a rating factor by examining the effect on the premium if the factor is omitted from the premium calculation process. The Average Class method calculates the weight of a rating factor by calculating the average differences of the discounts and surcharges associated with the factor. In order to position as accurate as possible an estimate of the effect of implementing either of these weighting methods, DOI created a large database to represent all of California's auto insurance consumers. This database contains detailed individual records from the top 11 auto insurer groups plus a major writer of substandard risks; in total, it included over 11 million records with information on each individual's driving record, annual mileage, years licensed, vehicle characteristics, use, ZIP code where garaged, coverage levels, premiums charged, and more. The database also included detailed information on the rating factors actually used by insurers.

DOI's analysis indicated that proper application of either weighting methodology in a revenue-neutral fashion to the 11 million consumers in its database would have "little average change in premium from what they currently pay. Most of the larger average changes occur at the extreme ends of the mileage groups (the very low mileage driver and the very high mileage drivers), and among the very young or inexperienced drivers. These changes seem to be consistent with the intent of Proposition 103. For both methods using the standardized factors, Los Angeles County averaged a reduction in premium of $7 to $8, while Sacramento and Fresno counties averaged increases of $13 to $14, and the San Francisco Bay Area averaged around a $4 increase."

In addition to its finding that Proposition 103 can be properly implemented without excessive premium shifts, DOI also made other findings, including the following:

- "Sequential analysis [the weighting method required by existing section 2632.7] does not result in the three mandatory factors having the effect on premium that Proposition 103 requires."
- None of the insurers analyzed are currently complying with the requirements that auto premiums be primarily determined by the safety record, mileage, and driving experience rating factors.
- The current underutilization of the mileage rating factor is the cause of the greatest amount of noncompliance with Proposition 103. If a rate has not yet been filed: or if the insurer is unable to show a sufficient increase in annual mileage is the single most important source of dislocation among all the rating factors.
- There is no way to change the current rating practices to come into compliance with Proposition 103 that is free of dislocation.
- Both of the two major approaches examined in this report result in "primarily positive or nil dislocation. The majority of increased premiums falls on those with the poorest safety records, less experience, and greater miles driven," while their opposites (i.e., lower-risk drivers) pay less.
- Standardization of the rating factors will "reduce the arbitrariness of the current rating process, level the playing field among the insurers, and allow the Department to more easily monitor compliance. Standardization of all factors would focus competition on strategies other than risk avoidance."

As noted, Commissioner Gillespie's "weighting methodology" regulation does not comply with Proposition 103, and Commissioner Garamendi failed to adopt a different one prior to leaving office. That task now rests with Commissioner Quackenbush, who has historically opposed Proposition 103 but promised to enforce it if elected. The new Commissioner will not be able to wait very long; at this writing, a coalition of consumer groups headed by the Proposition 103 Enforcement Project is drafting a petition requesting Quackenbush to commence the rulemaking process to adopt the regulations recommended by DOI in its December report.

Objective Rating Criteria for Non-Auto Lines of Insurance. On December 19, DOI held a public hearing on its proposal to adopt new sections 2360.0–2360.8, Title 10 of the CCR, to implement numerous provisions of existing law which state that premium rates in many lines of insurance shall not be "excessive, inadequate, or unfairly discriminatory." In auto insurance, Proposition 103 requires insurers to base rates on three mandatory factors and other optional factors as adopted by the Commissioner through rulemaking (see above); however, no objective rating criteria have been established for other lines of insurance, and no law or regulation states a method to avoid unfair discrimination in other rates or lines of insurance.

Thus, Commissioner Garamendi proposed to adopt "objective rating criteria" regulations. Section 2360.2 would require insurers to maintain objective criteria by which to evaluate all insureds and potential insureds for every subject line of insurance at every rate; any insured which satisfies the objective criteria would automatically qualify for that rate. Section 2360.3 would require insurers to inform insureds and applicants whether they qualify to purchase insurance and at what rate. Section 2360.4 would require an in-
surer to charge an insured the lowest rate for which the insured qualifies, and to adjust rates at each policy renewal so that an insured which is eligible for a rate reduction will be charged accordingly. Section 2360.5 would place responsibility for charging the appropriate rate on the insurer, not the agent or broker. Section 2360.6 would require insurers which are in the same “insurer group” and which offer the same insurance to charge the same rates. Section 2360.7 would require insurers to keep documentation indicating how they calculated each insured’s rate. Section 2360.8 would require insurers, when offering broadened or enhanced coverage to new insureds, to offer the same coverage to existing insureds.

Insurance industry representatives at the December 19 hearing attacked the “objective rating criteria” requirement as impossible to comply with and too costly. Hugo Gillis, representing surety insurance interests, argued that objective criteria cannot be determined due to subjective elements, including character, capacity, and conditions of the business to be insured. He stated that it is impossible for two consumers to have the same risk, and impossible to write comprehensive criteria. Gillis also argued that the regulations would expose insurance companies to increased liability for discriminatory treatment. Other witnesses made similar arguments, stating that experienced underwriters are needed to assess unique risks, and unique criteria are impossible to anticipate.

Commissioner Garamendi did not complete this rulemaking proceeding before leaving office. Commissioner Quackenbush put the proceeding on hold upon taking office; its status at this writing is unclear.

Industry Continues to Push Homeowners/Earthquake Insurance “Crisis.” By the end of 1994, the insurance companies which write 75% of homeowners insurance in California—including Allstate, California State Automobile association, Farmers, Safe, 20th Century, Prudential, CIG, Utica, and Foremost—announced they would sell no new policies. Two other companies—Cigna and Republic—are leaving the state. Still others—including State Farm, Southern California Automobile Association, Fireman’s Fund, Chubb, and Mercury—will write new policies only in certain geographic areas. With regard to renewal of existing policies, over 70 companies demanded rate increases during the fall—many by more than 100%.

The industry’s moratorium on the sale of homeowners’ insurance is due to “huge losses” alleged by the industry after paying claims resulting from the January 1994 Northridge earthquake. Since the quake, the industry has been demanding several legislative changes, the most important of which is the proposed “delinking” of homeowners and earthquake insurance which would be accomplished through the repeal of Insurance Code section 10081, which currently requires all insurers to sell homeowners insurance in California to also offer earthquake insurance. Insurers also seek enactment of a new state-backed earthquake insurance pool to replace the flawed and now-defunct Green-Hill-Areais-Farr California Residential Earthquake Recovery Fund initiated by the Deukmejian administration after the 1989 Loma Prieta earthquake [12:2&3 CRLR 173; 12:1 CRLR 121-22; 11:4 CRLR 134], and/or passage of federal legislation which would impose a surcharge on all homeowners policies (adjusted for regional risk of earthquakes, hurricanes, wildfires, or other catastrophes) to help cover claims resulting from natural disasters.

Consumer groups believe the industry is fabricating the “crisis” in order to persuade regulators to approve underserved rate increases. Last summer, a coalition of public interest organizations led by the Proposition 103 Enforcement Project asserted that the insurance industry’s “crisis” stems not from the Northridge earthquake but from several years of relatively low interest rates. “Insurance companies make most of their profit from the investment of the premiums we pay, not from the net proceeds of underwriting.” The coalition noted that, for 23 years (since the 1971 Sylmar earthquake), southern California homeowners have paid insurance premiums which include an annual 2-6% “catastrophic load factor” in anticipation of another severe seismic disturbance. Additionally, the groups asserted that insurance companies have been selling earthquake insurance at a price often equal to 50% of the cost of the regular homeowners policy and have insisted on deductibles that exclude coverage for all but the most severe quakes. “As a result, notwithstanding the complaints and machinations of the insurance industry, there is no company in California today that is unable to pay the claims arising from the Northridge earthquake.” The coalition called on legislators to delink insurance’s call on insurers to separately fund earthquake liabilities but will limit their profits. The industry wants a total delinking of lucrative homeowners insurance from risky earthquake policies, and is unhappy with a shared risk.

The issue remained unresolved when Garamendi left office. New Commissioner Quackenbush, who has stated that he supports delinking of earthquake and homeowners insurance if it can be accompanied by “protection for current earthquake policyholders,” was immediately greeted with a January 10 petition from the
consumer coalition, which repeated its contention that the "crisis" has been manufactured by the industry as an excuse to seek higher rates. The coalition pointed out that most companies have indicated they will still sell earthquake insurance (thus admitting that earthquakes are not "uninsurable") but only at exorbitant rates. The groups argued that there is no standard methodology for the setting of earthquake insurance rates, and different companies' methods appear to be completely arbitrary. The coalition urged Quackenbush to convene a series of public rulemaking and investigatory hearings for the purpose of determining the actual seismic risk in California and developing regulations which will govern how insurers set rates for earthquake coverage. If the hearings result in agreement that earthquakes are either uninsurable or impossible to scientifically or rationally rate, the coalition argued that DOI should hold further hearings to determine how to offer the public protection through the private marketplace in the short term while developing a long-term solution. Until DOI has conducted these hearings, the coalition called on Quackenbush to freeze earthquake insurance rates.

At this writing, Commissioner Quackenbush has not taken action on the coalition's petition; in the meantime, however, several legislators have introduced bills to repeal or suspend section 10081 (see LEGISLATION).

DOI Proposes to Overhaul CAARP Regulations. On December 9, the Department published notice of its intent to adopt new sections 2400–2441, Title 10 of the CCR; the new regulations will replace existing sections 2400–2454, the Department's rules governing the California Automobile Assigned Risk Plan (CAARP). CAARP, established by Insurance Code section 11620 et seq., is a program which is intended to equitably apportion among all insurers admitted to transact liability insurance those applicants for automobile bodily injury and property damage liability insurance who are in good faith unable to procure that insurance from an admitted insurer; eligible vehicles must be registered in California, with military exceptions. CAARP policies will provide the minimum coverage required by law; uninsured motorist coverage will be consistent with Insurance Code sections 11580.2 and 11580.26. The regulations also provide for the CAARP Advisory Committee, which includes seven members appointed by the Commissioner and eight members elected by the insurers participating in the Plan, and—consistent with Insurance Code section 11623(a)—specify the Advisory Committee's responsibilities to advise the Commissioner on matters affecting the operation of the Plan, including ratemaking, assignment procedures, appeals, and anti-fraud activities. The Advisory Committee must meet in public once per month under the provisions of the Bagley-Keene Open Meeting Act, and may appoint a Manager to perform administrative functions, receive and process applications, assign applicants to designated insurers, and respond to consumer inquiries.

At this writing, DOI is scheduled to conduct a public hearing on its proposed regulations on February 16 in San Francisco.

CAARP Producer Certification and Performance Standards. On November 11, the Department published notice of its intent to adopt new sections 2431.1, 2431.2, and 2431.3, Title 10 of the CCR, to implement SB 1721 (Johnston) (Chapter 1092, Statutes of 1994), which added new Insurance Code section 11622.5. The proposed regulations would establish a certification program whereby insurance producers (broker-agents licensed to transact automobile insurance in California) may become eligible to submit applications to CAARP (and be paid a commission by the Plan). The proposed regulations would also establish performance standards with which producers must comply in order to remain certified, and set forth recordkeeping and enforcement procedures with which the CAARP Manager must comply to detect and report producer violations to the CAARP Advisory Committee and the Commissioner.

According to DOI, the proposed regulations will facilitate uniformity and fairness in the operation of the Plan. Under the regulations, every insurer which has written automobile insurance after November 8, 1988 is obligated to participate in the Plan, because Insurance Code section 1861.02 (added by Proposition 103) imposes a continuing obligation unless the insurer has completely withdrawn from the state. Eligible applicants must be California residents who have a valid driver's license and are unable to obtain auto insurance from an admitted insurer; eligible vehicles must be registered in California, with military exceptions. CAARP policies will provide the minimum coverage required by law; uninsured motorist coverage will be consistent with Insurance Code sections 11580.2 and 11580.26. The regulations also provide for the CAARP Advisory Committee, which includes seven members appointed by the Commissioner and eight members elected by the insurers participating in the Plan, and—consistent with Insurance Code section 11623(a)—specify the Advisory Committee's responsibilities to advise the Commissioner on matters affecting the operation of the Plan, including ratemaking, assignment procedures, appeals, and anti-fraud activities. The Advisory Committee must meet in public once per month under the provisions of the Bagley-Keene Open Meeting Act, and may appoint a Manager to perform administrative functions, receive and process applications, assign applicants to designated insurers, and respond to consumer inquiries.

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REGULATORY AGENCY ACTION

bers and provide telephone and/or written price quotes for automobile insurance. The Department initiated the rulemaking proceeding in response to comments made at its October 1993 public investigative hearings on the high percentage of inaccurate quotes for private passenger automobile coverage. [14:4 CRLR 171; 14:1 CRLR 101; 13:4 CRLR 112–13]

As originally published, proposed section 2632.14.4 would require auto insurers to maintain toll-free telephone numbers for the purpose of providing price quotations to “good drivers” as defined in Insurance Code section 1861.025. To enable the insured to determine what coverages he/she has been quoted and what prices have been charged for the coverages, the section would further provide that when insurers and agents provide a good driver with a telephone price quote, they must tell the caller that he/she is entitled to an itemization of the price quote either by telephone or in writing, and must provide that itemization either orally or in writing as requested. The regulation would further require insurers to provide good drivers with a declarations page which sets forth the total price charged for the policy and an itemization of the total price charged, to enable the insured to determine what coverages he/she has been sold, what prices have been charged, and what fees, surcharges, discounts, and credits have been applied. Also on the declarations page, the insurer must list the mandatory and optional auto rating factors used in rating the policy (see above). Finally, the section would require insurers to honor written price quotes by providing coverage at the price and on the terms quoted until the date a rate change affecting the quote is approved by the Commissioner; insurers and agents must keep copies of written price quotes for six months.

The public hearings were dominated by two groups—Independent insurance agents and brokers, and Public Advocates, a San Francisco-based public interest organization representing non-English-speaking minority groups. The independent agents complained about most sections of the proposed regulation, including provisions which permit insurance companies to give direct quotes by phone (thereby bypassing independent agents and allegedly destroying their livelihood) and require insurers to provide quotes within two business days, tell callers of the limits and coverages required by law, provide an itemized quote (including the total price, the prices for different coverages, and what fees, surcharges, discounts, and credits have been applied), and honor their quote. DOI responded by modifying the language of the proposed regulation to provide insurers with an option of either directly providing quotes to a caller or referring the caller to a nearby agent, extending the response time to within three days of the caller’s initial request for a quote (or five days by mail), deleting the requirement to provide quotes with the limits and coverages required by law, deleting all requirements for itemization except as to fees and deductible, and watering down the “honor-orthy-quote” requirement. Under DOI’s modified language, only quotes which are “consistent with the insurer’s approved rates, rating plans, rating systems, and underwriting rules,” and which are provided to “good drivers” who are in fact “good drivers,” must be honored.

Public Advocates asked DOI to increase access to insurance through anti-redlining measures and increased availability of bilingual insurance agents. The organization estimated that seven million Californians of driving age speak a foreign language at home and need bilingual insurance agents to explain their options. Public Advocates noted that AT&T offers a translation service, and suggested that the insurance industry use it or develop its own multilingual program. The independent insurance agents in the audience replied that market forces should determine whether they should hire bilingual agents and where they should open branch offices. DOI compromised by adding a new subsection (m) to the proposed regulation, which states that “[a]ll insurers and agents subject to this regulation are referred to...[regulatory] section 2646.6(b)(5), which requires insurers to file a Community Service Statement with the Department of Insurance in which they state the number of their agents and claims adjusters who identify themselves as conversant in a language other than English. Consistent with section 2646.6(b)(5) and the goal of providing insurance and insurance services to all Good Drivers in California, insurers and agents are encouraged to provide toll-free telephone number service, application forms, claims forms, and other insurance services to the public in languages other than English, such as Spanish, Chinese, Tagalog, Korean, and Vietnamese.”

DOI released the modified language of proposed section 2632.14.4 on December 8 for a 15-day public comment period, and thereafter submitted the rulemaking file on the proposed regulation to OAL for approval. However, Commissioner Quackenbush withdrew the file from OAL upon taking office on January 3 (see above); at this writing, its status is unclear.

- Anti-Redlining Regulations. On October 7, OAL approved—with one exception—the remaining portions of section 2646.6, Title 10 of the CCR, Commissioner Garamendi’s revised regulation to discourage redlining in the provision of auto, homeowners, commercial, and fire insurance. [14:4 CRLR 124–25] OAL disapproved the Commissioner’s incorporation by reference of a 37-page “DOI Statistical Analysis Plan.” On December 7, DOI released a modified version of the Statistical Analysis Plan and modified language of section 2646.6; the purpose of the modifications, according to the Department, is to streamline the data gathering and reporting process required by the new regulation. Following a final written comment period ending on December 23, DOI submitted the revised rulemaking file to OAL. However, Commissioner Quackenbush withdrew the file from OAL upon taking office on January 3 (see above); at this writing, its status is unclear.

• Regulations to Prohibit Redlining in Surety Insurance. Following a May 1994 public hearing, DOI adopted new section 2646.7, Title 10 of the CCR, which is patterned after its generic anti-redlining regulations (see above) but focuses specifically on surety insurance. Among other things, section 2646.7 would require surety insurers to annually compile and report to the Commissioner specified information related to the number of applications received and granted for surety bonds for construction projects, the total number of surety bonds for construction projects provided to minority-owned firms, the total dollar amount of surety bonds issued for construction projects generally and for minority-owned firms. The Commissioner will compile these data on an annual basis and make the data on each surety insurer available for public inspection. The regulations define the term “minority” to mean American Indian or Alaskan Native, Asian or Pacific Islander, African-American, or Latino. [14:2&3 CRLR 130]

During the fall, DOI submitted the rulemaking file on proposed section 2646.7 to OAL for review and approval. However, Commissioner Quackenbush withdrew the file from OAL upon taking office on January 3 (see above); at this writing, its status is unclear.

• Minimum Reserve Standards for Disability Insurance. On November 4, OAL approved DOI’s adoption of new Article 3.5 (sections 2310–15), Title 10 of the CCR, which establishes specific minimum reserve standards for disability insurance. [14:4 CRLR 125; 14:2&3 CRLR 132–33] The proposed regulations set minimum reserve standards, inform insurers of the tests that will be used by the Commissioner to determine whether reserves are adequate, list
the elements that will be taken into account, set forth various actions which may be taken when inadequacy is found, provide for situations that are exceptions to the general rule, and name the three categories of reserves and require adequacy in each category.

- **Rulemaking to Implement AB 1672 (Margolin) Expires.** On January 4, DOI's emergency regulations to implement AB 1672 (Margolin) (Chapter 1128, Statutes of 1992) expired and were repealed by operation of law. AB 1672, which added sections 10198.6—9 and 10700-10749 to the Insurance Code, dramatically restructured California's market for health insurance for employees of "small employers." Emergency sections 2233-2233.99 (non-consecutive), Title 10 of the CCR—which had been readopted repeatedly by DOI under Commissioner Garamendi—defined key terms in the statute, clarified existing ambiguities in the law, and attempted to bring as many sources of health coverage as possible within the jurisdiction of AB 1672. These emergency regulations also reflected changes to AB 1672's small employer provisions (Insurance Code sections 10700-10718.6) made by bills enacted during 1993. [14:1 CRLR 104; 13:4 CRLR 113-14; 13:2&3 CRLR 132-33]

- **Workers' Compensation Regulations.** Before leaving office, Commissioner Garamendi adopted regulations implementing SB 30 (Johnston) (Chapter 228, Statutes of 1993), which repeals—effective January 1, 1995—the existing minimum rate system for workers' compensation insurance and replaces it with a competitive, "file and use" system (Insurance Code sections 11730-39). SB 30 was part of a seven-bill package which finally overhauled some of the more glaring defects in the workers' compensation system. [13:4 CRLR 115-16] Specifically, the Commissioner took the following actions [14:4 CRLR 124]:

  - In Proceeding RH-324, DOI adopted new sections 2509.30, 2509.31, 2509.32, 2509.33, and 2509.34, Title 10 of the CCR, on an emergency basis on October 13, to regulate how workers' comp insurers must file their rates, rating plans, and supplementary rating information with DOI, and specify the information which must be included in each filing and the procedures for their disapproval. The emergency regulations are valid for 120 days.

  - In Proceeding RH-325, DOI repealed sections 2350, 2353, 2318.5, and 2352.1, Title 10 of the CCR, the Department's minimum rate regulations under the old rating system, effective January 1, 1995.

  - Finally, in Proceeding RH-326, Commissioner Garamendi amended section 2350, Title 10 of the CCR, to reduce basic minimum workers' comp rates by approximately 16% on September 21. The rate decrease took effect on October 1.

- **Voters Reject Proposition 186.** On November 8, California voters rejected Proposition 186, a ballot initiative which proposed to replace existing private health insurance policies and public health care programs with a government-run, "single payer" health care program. The initiative, dubbed the California Health Security Act, would have provided lifetime medical coverage, including long-term care, and dental, vision, mental health, and prescription drug coverage, to all Californians. Currently, over six million Californians (80% of whom are employed or are family members of an employed person) are not covered by any form of health insurance because their employers do not provide health coverage, they earn too little to afford private coverage, and they earn too much to qualify for Medi-Cal. Political commentators attributed the outcome to voters' fears over the capability of the government to administer a health care system, and the need for increased taxes and/or threatened cuts in other programs (such as education and crime prevention) to finance the program.

### LEGISLATION

**AB 115 (McDonald).** Insurance Code section 10081 provides that no policy of residential property insurance may be issued or delivered or, under certain circumstances, initially renewed by any insurer unless the named insured is offered coverage for loss or damage caused by an earthquake. Under existing law, an insurer may not refuse to renew, reject, or cancel a policy of residential property insurance solely because the insurer has accepted earthquake coverage. As introduced January 11, this bill would provide instead that it is an unfair business practice for an insurer to refuse to renew, reject, or cancel a policy of residential property insurance that includes coverage for the peril of earthquake because the insurer has accepted earthquake coverage; provide that it is an unfair business practice for an insurer to cancel a policy of residential property insurance solely because the insurer has accepted earthquake coverage. As introduced January 11, this bill would provide instead that it is an unfair business practice for an insurer to require, as a condition for the renewal of a policy of residential property insurance that includes coverage for the peril of earthquake, that the insured agree to accept residential property coverage that does not include coverage for the peril of earthquake; provide that it is an unfair business practice for an insurer to transfer its existing risk of earthquake insurance to the California FAIR Plan, unless the Commissioner finds that the insurer's potential exposure to losses threatens the solvency of the insurer and expressly authorizes the transfer; and provide for a fine of $10,000 by the Insurance Commissioner for a violation of each of these provisions. [A. Ins]

**SB 58 (Lewis),** as introduced December 28, would exempt insurers from complying with Insurance Code section 10081 from the effective date of the bill until the Insurance Commissioner certifies to the Secretary of State that, in the Commissioner's opinion, federal legislation has been enacted that creates a nationwide program that adequately insures losses due to earthquake. In addition, the bill would provide that for policies sold prior to the effective date of the bill or after certification by the Commissioner, if an offer of earthquake coverage is accepted, the coverage must be continued only for the policy term, provided the residential property insurance policy is not cancelled by the named insured or the insurer.

Existing law provides that an insurer may not refuse to renew, reject, or cancel a policy of residential property insurance after an insurer has accepted an offer of earthquake insurance solely because the insurer has accepted that offer, unless the policy is terminated by the insurer. This bill would provide that an insurer may refuse to renew or cancel a policy if the decision to cancel or refuse is based on sound underwriting principles, if the Commissioner finds that the exposure to potential losses will threaten the solvency of the insurer, if the insurer has a reduced opportunity to obtain reinsurance, or for other specified grounds for cancellation. [S. Ins]

**AB 13 (McDonald),** as introduced December 5, would—among other things—make legislative findings relative to insurers and the provision of earthquake insurance, and suspend, for a limited period of time, Insurance Code section 10081's requirement that earthquake insurance be offered with homeowners insurance. The bill would also provide that an insurer may not cancel or refuse to renew in specified instances. This provision would be repealed as of January 1, 1998. The bill would provide that the Department of Insurance shall, at the Commissioner's discretion or on the request of a consumer or homeowners' group, conduct a survey of the availability of earthquake
insurance for residential property. The Commissioner shall make this information available, as specified. The bill would require the Commissioner to authorize the formation of a market assistance program, in which insurers, agents, and brokers may participate on a voluntary basis to assist in securing earthquake insurance for loss or damage to residential property. A homeowner would be required to have an agent or broker certify that no coverage is available to the homeowner as a condition of obtaining coverage through the plan.

This bill would also authorize the California FAIR Plan Association to provide earthquake property insurance coverage. The bill would provide guidelines for FAIR’s governing board to set rates for earthquake insurance coverage, and provide that loss and risk of loss shall be allocated in the same manner as under the California FAIR Plan. The bill would also provide limitations on the coverage that can be offered through the program. These provisions would be repealed on January 1, 1998.

This bill would also permit insurers to reduce the coverage contained in existing policies providing earthquake insurance coverage to coverage comparable to that provided under the earthquake program of the California FAIR Plan, on specified notice to insureds. [A. Ins]

AB 8 (Friedman). Existing law imposes various requirements on insurers and health care service plans (HCSPs) with respect to small employer coverage. Among other things, HCSPs and insurers that sell coverage to small employers are required to make available coverage to all small employers. For that purpose, small employers are employers that employ at least three, but no more than 50, eligible employees. As introduced December 5, this bill would expand the definition of small employers to mean employers that employ at least one, but no more than 100, eligible employees. This bill would also require HCSPs and insurers to sell all of the small employer contracts or plan designs to individuals as well as small employers. [A. Health]

AB 73 (Friedman). The Knox-Keene Health Care Service Plan Act of 1975 provides for the licensure and regulation of HCSPs by the Commissioner of Corporations; the Insurance Code provides for the regulation of policies of disability insurance by the Insurance Commissioner. Existing law requires that HCSP contracts and disability insurance policy contracts must contain certain provisions. Willful violation of the Knox-Keene Health Care Service Plan Act of 1975 or related regulations is a misdemeanor. As introduced December 21, this bill would prohibit HCSPs and disability insurers from awarding bonus compensation to any employee on the basis of that employee’s performance in denying authorization or payment for costly services. [A. Health]

SB 87 (Kopp). Existing law provides that the written consent of the Attorney General is required prior to the employment of counsel for representation of any state agency or employee in any judicial proceeding. There is an express exception provided to specified state agencies and to the Insurance Commissioner with respect to certain delinquency proceedings. As introduced January 10, this bill would delete the exception provided to the Commissioner and remove the specific authority of the Commissioner to employ counsel in connection with delinquency proceedings. This bill would also make legislative findings that it is in the best interest of the state that the Attorney General be provided with the resources needed to perform specified duties, and would require the Attorney General, upon request of the Commissioner, to petition the court for determination in the event the Commissioner and the Attorney General disagree as to the need to employ counsel outside of state service or the compensation of that counsel. [S. Jud, S. Ins]

LITIGATION

On December 23, 20th Century Insurance Company filed a petition for a writ of certiorari to the U.S. Supreme Court, seeking review of the California Supreme Court’s unanimous decision upholding former Commissioner John Garamendi’s Proposition 103 rollback regulations in 20th Century Insurance Company v. Garamendi, 8 Cal. 4th 216 (Aug. 17, 1994). [14:4 CRLR 129-31] With the change of Commissioner, the case is known in the Supreme Court as 20th Century Insurance Company v. Quackenbush, No. 94-1119. 20th Century primarily argues that the application of the formula in Commissioner Garamendi’s rollback regulations would effect a taking of its property rights because the formula fails to afford it an opportunity to recover its reasonable expenses and costs of capital. The insurer contends that the California Supreme Court applied the wrong legal standard in considering its confiscation claim. Whereas the California Supreme Court required 20th Century to allege and prove “deep financial hardship” in support of its confiscation claim (and found that 20th Century met the test), 20th Century contends that Federal Power Commission v. Hope Natural Gas Company, 320 U.S. 591 (1944), and Guaranty National Insurance Company v. Gates, 916 F.2d 508 (9th Cir. 1990), permit a lesser showing of harm in order to state a takings claim.

On behalf of the Commissioner, attorneys Fredric Wooncher and Michael Strumwasser urged the Court to deny 20th Century’s petition, noting that the company enjoyed a 31.5% rate of return on its statutory equity in 1989 and that application of the rollback regulations requires it to refund 12.203% of its 1989 premiums; in other words, according to Wooncher and Strumwasser, 20th Century is contending that it is constitutionally entitled to a one-year rate of return of at least 20%. The Santa Monica attorneys also accused 20th Century of fabricating a conflict among the courts on the appropriate legal standard and of misinterpreting the California Supreme Court’s decision.

Another major Proposition 103 case is still pending before the California Supreme Court. In Amwest Surety Insurance Company v. Wilson, 20 Cal. App. 4th 1275 (Dec. 8, 1993), the Second District Court of Appeal struck down a 1990 statute exempting surety companies from the rollback and prior approval provisions of Proposition 103 because it does not “further the purposes” of the initiative and is thus beyond the authority of the legislature. [14:2 & 3 CRLR 129; 14:1 CRLR 108; 13:2 & 3 CRLR 130] At this writing, the case is being briefed and no date for oral argument has been set.

On October 13, the California Supreme Court granted the insurance industry’s petition for review of the First District Court of Appeal’s decision in Manufacturers Life Insurance Company, et al v. Superior Court (Well Insurance Agency, Real Party in Interest), 27 Cal. App. 4th 67 (July 29, 1994). In that decision, the First District held that an insurance brokerage may not bring a private cause of action for redress of an unlawful group boycott under the Unfair Insurance Practices Act (UIPA), Insurance Code section 790 et seq., but it may pursue antitrust remedies under the Cartwright Act, Business and Professions Code section 16720 et seq., and injunctive and restitutionary relief under the Unfair Competition Act (UCA), Business and Professions Code section 17200 et seq. [14:4 CRLR 131; 14:2 & 3 CRLR 139]

Plaintiff Weil was a broker of and consultant on a form of life insurance known as “settlement annuities”; a settlement annuity is an annuity purchased by a liability carrier to fund a settlement (a periodic payment) settlement in a personal injury action. It was plaintiff’s practice to advise and educate injury claimants and their attorneys with information concerning the underlying features of settlement annui-
ties, in particular their actual costs. According to the court, “[s]uch disclosures were inimical to a plan defendants had formed to market settlement annuities as a way for liability carriers to settle injury claims below their cash settlement value.” Thus, defendants allegedly coerced and induced suppliers of annuities to stop doing business with plaintiff; as a result, plaintiff’s business was destroyed.

Weil brought suit against the insurers, asserting (among other things) statutory claims under the UIPA, the Cartwright Act, and the UCA. The trial court sustained defendants’ demurrers on the Cartwright Act claims, but concluded that Weil had stated claims under the UIPA and the UCA. Defendants appealed.

The primary issue on appeal was the insurers’ contention that the UIPA, which prohibits acts of “boycott, coercion, or intimidation resulting in or tending to result in unreasonable restraint of, or monopoly in, the business of insurance,” “supplants the Cartwright Act and the UCA so as to provide the sole basis by which unlawful conduct of the type alleged here may be subject to legal restraint or may otherwise produce legal consequences.” The court noted that the UIPA itself “expresses an affirmative intention and expectation that it will preserve intact existing remedies for insurance industry misconduct,” and observed that “[i]f the legislature wished to exempt the insurance industry from the Cartwright Act, it knew full well how to do so.” Additionally, the court “observe[d] a certain illogic in referring to the UIPA as providing an ‘exclusive remedy’ when.. .it provides no private remedies for insurance industry misbehavior.”

The Department regularly publishes three bulletins. The Real Estate Bulletin, which is circulated quarterly as an educational service to all current licensees, contains information on legislative and regulatory changes, commentaries, and advice; in addition, it lists names of licensees who have been disciplined for violating regulations or laws. The Mortgage Loan Bulletin is published twice yearly as an educational service to licensees engaged in mortgage lending activities. Finally, the Subdivision Industry Bulletin is published annually as an educational service to title companies and persons involved in the building industry.

The California Association of Realtors (CAR), the trade association joined primarily by agents and brokers working with residential real estate, is the largest such organization in the state. CAR is the largest such organization in the state. CAR is often the sponsor of legislation affecting DRE. The four public meetings required to be held by the Real Estate Advisory Commission are usually scheduled on the same day and in the same location as CAR meetings.

At this writing, DRE Chief Deputy Commissioner John Liberator continues to serve as Interim Commissioner, following the resignation of former DRE Commissioner Clark Wallace.

MAJOR PROJECTS

DRE Disciplines Two Prepaid Rental Listing Services. In the wake of dozens of consumer complaints and lawsuits, DRE has reprimanded two San Fernando Valley rental listing services; in December, DRE issued desist and refrain orders to Valley Rental of Burbank. The main subject of consumer complaints is alleged misrepresentation by the services regarding tenancy availability and lease terms.

In sales, or leases exceeding one year in length, of any new residential subdivisions consisting of five or more lots or units, DRE protects the public by requiring that a prospective purchaser or tenant be given a copy of the “public report.” The public report serves two functions aimed at protecting purchasers (or tenants with leases exceeding one year) of subdivision interests: (1) the report discloses material facts relating to title, encumbrances, and related information; and (2) it ensures adherence to applicable standards for creating, operating, financing, and documenting the project. The commissioner will not issue the public report if the subdivider fails to comply with any provision of the Subdivided Lands Act.